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National**Economic**Trends

Growth and the Current Account Deficit

The U.S. current account deficit grew at an average annual rate of 9 percent between 1990 and 1997 increasing from $77.0 billion to $140.5 billion. By the end of 1999, the deficit had surged to $331.5 billion, an annual increase of nearly 54 percent over two years. What explains this sharp increase? The simple answer is that the U.S. economy continued to grow strongly during 1998 and 1999, while the economies of some of our key trading partners contracted.

The table shows the main components of the current account balance. The second and third rows show the difference between U.S. exports and imports of goods and services, respectively. The balance on income has two parts: the difference between returns on U.S. investments in other countries and returns earned by foreigners on investments in the United States, and the difference between compensation paid to U.S. workers abroad and foreign workers in the United States. Net unilateral transfers consist primarily of U.S. grants to foreign countries and private remittances.

The growth rate of U.S. imports depends in part on the growth of the U.S. economy, whereas the growth rate of U.S. exports depends in part on the growth of foreign output. As income rises, individuals and businesses increase their purchases of both domestic and foreign produced goods. Between 1990 and 1997, U.S. imports of goods rose by 8.4 percent annually. The annual growth rate of goods exports was only slightly lower at 8.3 percent. Goods imports continued to grow at an annual rate of 8.4 percent between 1997 to 1999, as U.S. growth remained strong, but the average annual growth rate of exports fell to 0.3 percent.

The Asian crisis is largely responsible for this change. As a result of the crisis, exports of goods to Asia declined by 12 percent during 1998. Exports to the four countries most affected by the crisis (Korea, Indonesia, Malaysia and Thailand) fell by 31 percent. U.S. goods exports to Asia increased in 1999 but were below 1995 levels.

Service exports also declined in 1998, led by a fall in travel and transportation receipts. Visitors to the United States from Asia declined by 14 percent. In addition, the decline in goods shipments resulted in smaller freight revenues.

The Asian financial crisis and a subsequent slowdown in growth in Latin America also affected the balance on income. There was both a shift in the flow of assets toward the United States and an increase in the return on assets in the United States relative to returns abroad. Thus, in 1998, for the first time during the postwar period, payments to foreigners on investments in the United States exceeded U.S. receipts on foreign investment. This difference increased in 1999. In addition, earnings of U.S. companies operating abroad fell during 1998 and remained below pre-crisis levels in 1999.

A continued improvement in the world economy should raise the growth rate of U.S. exports and the return on U.S. investment abroad. A slowdown in growth in the United States should lower the growth rate of imports and reduce both the return on, and inflows of, investment in the United States. Either of these scenarios should reduce the U.S. current account deficit. However, so long as growth in the United States remains above that of our major trading partners, large deficits are likely to remain.

—Patricia S. Pollard

U.S. Current Account – Major Components
$ billions

	1997	1998	1999
Balance on Current Account	-140.5	-217.1	-331.5
Balance on Goods	-196.7	-246.9	-345.6
Balance on Services	90.7	80.0	80.1
Balance on Income	6.2	-6.2	-18.5
Net unilateral transfers	-40.8	-44.0	-48.0

Source: U.S. Department of Commerce, Bureau of Economic Analysis